

operating a payphone business unit. In summary, any incremental cost study is not representative of the total cost of providing payphone calls and should not be used as a proxy for the cost of providing payphone service. For example, MCI excludes certain software costs "because these costs do not vary with the number of payphones installed."³ Similarly, MCI includes only "variable overhead" in their calculation and excludes all fixed overhead expenses. Despite these costs not fluctuating with the installation of additional payphones, they are essential to the provision of payphone service and should be included in calculating the total or fully embedded per-call cost. We have revised the MCI study to include all costs of providing payphone service.

- The Average Number of Payphone Calls is Overstated: Coalition call counts (478 total calls per month⁴) are lower than those used in the MCI study (700 calls per month⁵). Considering Coalition payphones account for approximately 70%⁶ of all payphones, the call figures provided by the Coalition are more representative of the payphone industry. We have revised the MCI study using the Coalition-provided data.
- Costs Unique to PCC Calls are Excluded: As discussed in our July 13, 1998, report, there are several cost categories associated exclusively with PCC-eligible calls.⁷ Many of these costs, specifically interest on delayed PCC payments, additional PCC collection costs and PCC uncollectible costs, were excluded from the MCI study. We have revised the MCI study to include these cost categories.⁸

³ Id., at pg. 2.

⁴ See, Reply Comments of the RBOC/GTE/SNET Payphone Coalition, "Critique of Cost Studies and Other Issues", Carl R. Geppert (September 9, 1997), at pg. 5 [hereinafter "Andersen September 9, 1997 Report"].

⁵ See, MCI Study, at pg. 1.

⁶ See, Comments of the RBOC/GTE/SNET Payphone Coalition, "Report of Arthur Andersen on Per-Call Compensation", Carl R. Geppert (July 13, 1998), at pg. 10 [hereinafter "Andersen July 13, 1998 Report"].

⁷ Id., at ppg. 4-7.

⁸ Using Coalition call counts for PCC-eligible calls.

- The Average Investment and Capital Costs are Understated: The MCI study understates the capital costs of providing payphone service for the following reasons:
 - Based upon data provided by those Coalition members currently using large numbers of smart sets, the smart station investment figure used in the MCI study (\$985)⁹ is understated. For example, none of these Coalition members use the Dura-Smart phone which, according to MCI, has a cost of \$439 (after applying MCI's suggested 20% purchase discount).¹⁰ Conversely, the gross investment cost of deployed smart sets for these Coalition members ranges from \$1,000 to approximately \$1,300 (net of discounts).
 - It appears that the enclosure/pedestal investment figure used in the MCI study (\$333)¹¹ is understated. In our September 9, 1997, report in which we critiqued AT&T's coinless set cost study, we suggested that the average enclosure cost was \$725.¹² After speaking with Coalition members regarding enclosure costs, it appears that this cost estimate is reasonable. For example, one Coalition member with a large number of deployed smart sets has pedestal/enclosure costs ranging from \$515 to \$1,054 (simple average of \$785).
 - MCI understates the total capital cost of providing payphone service by excluding general support assets from the overall investment calculation (e.g., land, buildings, motor vehicles, etc.). The cost of these assets must be included considering the payphone business unit could not function without them.

Consequently, we revised the MCI study by substituting the FCC's estimate of total payphone investments taken from Peoples Telephone Company's and Communications

⁹ See, MCI Study, at pg. 7.

¹⁰ See, MCI Study, Attachment 1, at pg. A1-1. The Dura-Smart phone is valued at \$549. Applying the suggested 20% purchase discount results in an investment cost of \$439.

¹¹ See, MCI Study, at pg. 7.

¹² See, Andersen September 9, 1997 Report, at pg. 6.

Central, Inc.'s financial statements (\$3,234 and \$2,799 for an average of \$3,017).¹³

- Local Usage Expenses are Overstated: As discussed in our July 13, 1998, report, many payphone service providers ("PSPs") do not incur usage charges on local coin calls. Using the average per-call usage charge noted in our July 13th report (\$0.025 - \$0.03)¹⁴, which agrees with the FCC's estimate of per-call local usage costs, we re-computed the total usage costs per station, using Coalition local coin call counts, to be \$7.00 - \$8.40 per month (average of \$7.70). We revised the costs in the MCI study downward to incorporate a lower per-station usage cost.
- Universal Service Fund Expenses are Overstated: MCI incorrectly computed the Universal Service Fund ("USF") expenses associated with revenue generated from the average payphone.
 - USF is applied only to revenue collected from the end-user. In the majority of cases, this equates to coin revenue for Coalition PSPs. MCI, however, computes the 0.75% portion of USF based upon the total revenue generated from the average Peoples Telephone Company payphone (\$243.99 per month¹⁵). This figure includes much more than coin revenue. In fact, non-coin revenue accounts for approximately 33%¹⁶ of the total revenue. Including only coin revenue in the 0.75% calculation reduces the USF charge to \$1.22 per month.
 - MCI does not provide support for their assumption that 20% of all revenue is generated

¹³ See, Second Report and Order Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, 13 FCC Rcd 1778, 1802-03 (1997), at 106. The per-station capital cost was computed using a 15.76% rate of return and a 10-year depreciable life.

¹⁴ See, Andersen July 13, 1998 Report, at pg. 3.

¹⁵ See, MCI Study, at pg. 4; See, Peoples Telephone Company, Inc., Form 10-K (December 31, 1997), at pg. 25 [hereinafter "PTC's 10-K"].

¹⁶ See, PTC's 10-K, at pg. 24.

from interstate and international calls¹⁷. Based upon Coalition call data, less than 1% of all coin calls from payphones are interLATA. A more reasonable expense associated with the 3.14%¹⁸ interstate USF charge is \$0.05.

We have revised the USF expense in the MCI study taking into account the changes noted above.

- Total Overhead Expenses are Understated: The MCI study includes only variable overhead (i.e., general administrative expenses that fluctuate with the number of payphones installed). As discussed above, most PSPs' administrative expenses are fixed and do not fluctuate with the volume of installed payphones. All administrative costs must be included in the payphone cost calculation in order to compute the fully embedded cost of providing payphone service. As discussed in our September 9, 1997, report, Coalition data suggests that the average administrative expense per payphone is double the amount indicated in the MCI study (\$23 per month).¹⁹ We have revised the MCI study to incorporate all administrative costs associated with providing payphone service.
- Premise Owner Commissions are Excluded: MCI inappropriately excludes the cost of commissions in the per-station calculations. Commission costs are volume sensitive (i.e., incremental) and are generally accepted as a component of incremental cost studies. But for these payments to the location provider for the use of their facilities, payphone services could not be provided. Consequently, we have included an estimate for commission costs per station, based upon data provided by the Coalition (using commission rates applicable to local and toll revenue). Including commission costs in our calculation is appropriate because we are computing the cost per call on the average payphone, not a marginal

¹⁷ See, MCI Study, at pg. 4.

¹⁸ Id.

¹⁹ See, Andersen September 9, 1997 Report, at pg. 8.

payphone.

The following table compares the MCI study with our revised calculations:

<u>Cost Category</u>	<u>MCI Smart Set Payphone Cost Study</u>	<u>Revised Calculation</u>
Total Capital Costs per Payphone	\$26.72	\$46.93
<u>Volume Sensitive Costs</u>		
Usage	15.590	7.700
Interest on Delayed PCC Payments	NA	1.705
PCC Uncollectible Costs	NA	2.868
USF	3.360	1.269
	<u>18.950</u>	<u>13.542</u>
<u>Station Sensitive Costs</u>		
Monthly Line Charge	34.670	34.670
Payphone Line Coding	1.460	1.460
Maintenance & Repair/Coin	22.660	22.660
Collections & Counting		
Additional PCC Collection Costs	NA	0.659
	<u>58.790</u>	<u>59.449</u>
<u>Other Costs</u>		
Administrative Expenses	10.860	23.000
Commissions	NA	35.730
	<u>10.860</u>	<u>58.730</u>
Total Station Costs	\$115.320	\$178.651
Average Number of Calls	700	478
Average Cost Per Call (all calls)	\$0.165	\$0.374

SECTION II: NYNEX's NEW YORK INCREMENTAL COST STUDY IS NOT REPRESENTATIVE OF THE FULLY EMBEDDED COST OF OPERATING PAYPHONES

We were asked to determine whether the per call cost figures presented in New York Telephone's February 21, 1997, submission to the State of New York Department of Public Service ("the NYNEX study") are representative of the fully embedded costs of providing

payphone services. Many of our comments regarding the NYNEX study are similar to those made earlier in this proceeding with regard to cost figures presented by New England Telephone and Telegraph Company in its petition for increased local coin rates in the state of Massachusetts.²⁰ This methodology was used by NYNEX to show that a subsidy did not exist in a regulated environment. However, incremental cost studies are not representative of the total cost of providing payphone calls and should not be used as a proxy for total payphone costs.

Moreover, the cost figures presented in the NYNEX study (or lack thereof) do not represent the full cost of operating in a deregulated environment. For example, all line-related charges are stated at cost rather than at tariffed rates (Attachment H to the NYNEX study shows that the "Link/Port/Coin Functionality" amounts represent costs). In addition, the NYNEX study excludes many fixed costs associated with providing payphone service. Had NYNEX included the line-related charges at tariffed rates and all fixed administrative expenses, the per-call costs would have increased significantly.

ARTHUR ANDERSEN LLP



by

Carl R. Geppert

²⁰ See, Andersen September 9, 1997 Report, at ppg. 2-4.

CERTIFICATE OF SERVICE

I hereby certify that on this 27th day of July, 1998, I caused copies of the foregoing RBOC/GTE/SNET Payphone Coalition's Reply Comments on Remand Issues to be served upon the parties on the attached service list by first-class mail.


Marilyn Leeland

Federal Communications Commission
Service List

Federal Communications Commission

Christopher Wright
Laurence N. Bourne
John Edward Ingle
Federal Communications Commission
1919 M Street, N.W.
Washington, D.C. 20554

United States Department of Justice

Catherine G. O'Sullivan
Nancy C. Garrison
U.S. Department of Justice
Antitrust Division, Appellate Section
Patrick Henry Building
601 D Street, N.W., Room 10535
Washington, D.C. 20530

Robert B. Nicholson
Robert J. Wiggers
U.S. Department of Justice
Antitrust Division, Appellate Section
Patrick Henry Building
601 D Street, N.W., Room 10535
Washington, D.C. 20530

Donald J. Russell
U.S. Department of Justice
Antitrust Division, City Center Building
1401 H Street, N.W., Suite 8000
Washington, D.C. 20001

Airtouch Paging

Mark A. Stachiw
Airtouch Paging
12221 Merit Drive, Suite 800
Dallas, TX 75251

Airtouch Paging

Carl W. Northrop
Emmett A. Johnston
Paul, Hastings, Janofsky & Walker
1299 Pennsylvania Avenue, N.W.
10th Floor
Washington, D.C. 20004-2400

American Public Communications Council

Albert H. Kramer
Robert F. Aldrich
Christopher T. McGowan
Dickstein, Shapiro, Morin & Oshinsky, LLP
2101 L Street, N.W.
Washington, DC 20037-1526

AT&T

Peter D. Keisler
Sidley & Austin
1722 I Street, N.W., Suite 600
Washington, D.C. 20006

AT&T

Mark C. Rosenblum
Richard H. Rubin
AT&T Corporation
295 North Maple Avenue
Room 3252I3
Basking Ridge, NJ 07920

Cable & Wireless, Inc.

Rachel J. Rothstein
Cable & Wireless, Inc.
8219 Leesburg Pike
Vienna, VA 22182

Citicorp Service Inc.

Mark MacKenzie
Citicorp Service Inc.
8430 West Bryn Mawr Avenue
Chicago, IL 60631

Competitive Telecommunications Association

Genevieve Morelli
Competitive Telecommunications Assn.
1900 M Street, N.W., Suite 800
Washington, D.C. 20036

Competitive Telecommunications Association

Danny E. Adams
Steven A. Augustino
John J. Heitmann
Kelley Drye & Warren, LLP
1200 19th Street, N.W., Suite 500
Washington, D.C. 20036

Consumer-Business Coalition for Fair
Payphone-800 Fees

Howard J. Symons
Sara F. Seidman
Yaron Dori
Mintz, Levin, Cohn, Ferris, Glovsky
and Popeo, PC
701 Pennsylvania Avenue, N.W.
Washington, DC 20004-2608

Consumer-Business Coalition for Fair
Payphone-800 Fees

Daniel R. Barney
Robert Digges, Jr.
ATA Litigation Center
2200 Mill Road
Alexandria, VA 22314

Excel Telecommunications, Inc.

Dana Frix
Pamela S. Arluk
Swidler & Berlin
3000 K Street, N.W., Suite 300
Washington, D.C. 20007-5116

Excel Telecommunications, Inc.

James M. Smith
Excel Telecommunications, Inc.
1133 K Street, N.W., Suite 750
Washington, D.C. 20036

Frontier Corporation

Michael J. Shortley III
Frontier Corporation
180 S. Clinton Avenue
Rochester, NY 14646

International Telecard Association

Glenn B. Manishin
Michael D. Specht
Blumenfeld & Cohen
Technology Law Group
1615 M Street, N.W., Suite 700
Washington, D.C. 20036

IXC Communication Services, Inc.

Gary L. Mann
IXC Long Distance, Inc.
1122 Capital of Texas Highway South
Austin, TX 78746

LCI International Telecom Corporation	Brad E. Mutschelknaus Steven A. Augustino Kelley Drye & Warren LLP 1200 19 th Street, N.W., Suite 500 Washington, D.C. 20036
MCI Telecommunications Corporation	Mary J. Sisak Mary L. Brown George S. Ford MCI Telecommunications 1801 Pennsylvania Avenue, N.W. Washington, DC 20006
State of New York Department of Public Service	Lawrence G. Malone New York State Dept. of Public Service Three Empire State Plaza Albany, NY 12223-1350
Paging Network, Inc.	Judith St. Ledger-Roty Wendy I. Kirchick Kelley Drye & Warren LLP 1200 19 th Street, N.W., Suite 500 Washington, D.C. 20036
Personal Communications Industry Association	Robert L. Hoggarth Personal Communications Industry Assn. 500 Montgomery Street, Suite 700 Alexandria, VA 22314
Personal Communications Industry Association	Scott Blake Harris Kent D. Bressie Harris, Wiltshire & Grannis, LLP 1200 18 th Street, N.W., Suite 1200 Washington, D.C. 20036
PocketScience	Neil M. Peretz PocketScience Inc. 2075 de La Cruz Boulevard, Suite 200 Santa Clara, CA 95050

SkyTel Communications, Inc.

Thomas Gutierrez
J. Justin McClure
Lukas, Nace, Gutierrez & Sachs
1111 19th Street, N.W., Suite 1200
Washington, DC 20036

Sprint Corporation

Leon M. Kestenbaum
Jay C. Keithley
H. Richard Juhnke
Sprint Corporation
1850 M Street, N.W., 11th Floor
Washington, D.C. 20036

VoCall Communications Corp. and
Galaxy Long Distance

Thomas K. Crowe
Law Offices of Thomas K. Crowe, PC
2300 M Street, N.W., Suite 800
Washington, DC 20037

WorldCom, Inc.

Richard S. Whitt
WorldCom, Inc.
1120 Connecticut Avenue, N.W.
Suite 400
Washington, D.C. 20036

WorldCom, Inc.

Douglas F. Brent
WorldCom Inc.
101 Bullitt Lane, Suite 101
Louisville, KY 40222

July 27, 1998